

***United States Court of Appeals  
for the Second Circuit***



**BRIEF FOR  
APPELLANT**



ORIGINAL WITH AFFIDAVIT OF MAILING

# 76-5026

## United States Court of Appeals

FOR THE SECOND CIRCUIT

Docket No. 76-5026

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IN RE

BANQUE DE FINANCEMENT, S.A.,

*Debtor.*

BANQUE DE FINANCEMENT, S.A.,

*Appellant,*

P/S

FIRST NATIONAL BANK OF BOSTON,

and

CHASE MANHATTAN BANK, N.A.,

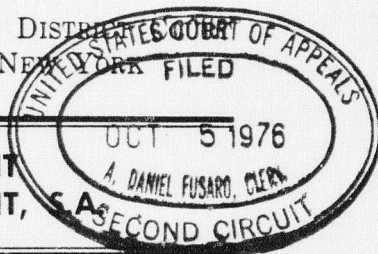
*Appellees,*

FIRESTONE TIRE AND RUBBER COMPANY,

*Intervenor in support  
of appellant.*

ON APPEAL FROM THE UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK

**BRIEF FOR APPELLANT  
BANQUE DE FINANCEMENT, S.A.**



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**BRIEF FOR APPELLANT  
BANQUE DE FINANCEMENT, S.A.**

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**Preliminary Statement**

Appellant Banque de Financement, S.A., ("Finabank") appeals from an order of the United States District Court for the Southern District of New York (Ward, J.), entered July 29, 1976, affirming an order of Bankruptcy Judge (Babitt, J.), dismissing the petition

filed by appellant under Chapter XI of the Bankruptcy Act, 11 U.S.C. §§ 701-799.<sup>1</sup>

The Chapter XI petition was dismissed despite this Court's recent decision that a bankruptcy court may not refuse to exercise jurisdiction over the assets of a foreign bank which, like Finabank, does not do business in this country. *Israel-British Bank (London) Ltd. v. FDIC*, 536 F.2d 509 (2d Cir. 1976), *petitions for cert. pending*, 45 U.S.L.W. 3203-04 (U.S., filed Aug. 23, 1976) (Nos. 76-271 & 272). The dismissal of the petition validates two enormous preferential liens obtained by the appellees, First National Bank of Boston ("FNBB") and The Chase Manhattan Bank, N.A. ("Chase") and deprives all the other American and foreign creditors of Finabank of any recovery—a result totally antagonistic to the policy and purpose of the Bankruptcy Act.

The courts below, however, conceived that under the circumstances of this case there was "discretion" to dismiss the case. This "discretion" supposedly derived from the construction of several provisions in the Bankruptcy Act and Rules, and a claimed "inherent power" within the court. It is submitted, however, that there is, as a matter of law, no discretion in the court to discriminate against certain creditors based on their nationality or situs of operations. In balancing whether to protect "local" creditors or whether to treat all creditors equally, the bankruptcy courts should have no choice but to find for equality of treatment among all creditors of the same class.

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<sup>1</sup> The opinions below have been reproduced in the Joint Appendix, references to which will be preceded by "App." Judge Ward's opinion appears at App. 277. Judge Babitt's opinion appears at App. 220.

### **Issue Presented for Review**

Did the lower courts err in dismissing Finabank's Chapter XI petition, while at the same time, refusing to adjudicate Finabank a bankrupt under Chapter VII, when the sole justification for refusal to adjudicate was to grant a preference to "American" creditors?

### **Statutes and Rules Involved (Bankruptcy Act and Rules)**

#### **STATUTES:**

Section 2. [11 U.S.C. § 11] Creation of Courts of Bankruptcy and Their Jurisdiction. a. The courts of the United States hereinbefore defined as courts of bankruptcy are hereby created courts of bankruptcy and are hereby invested, within their respective territorial limits as now established or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this Act, in vacation, in chambers, and during their respective terms, as they are now or may be hereafter held, to—

\* \* \* \* \*

(22) Exercise, withhold, or suspend the exercise of jurisdiction, having regard to the rights or convenience of local creditors and to all other relevant circumstances, where a bankrupt has been adjudged bankrupt by a court of competent jurisdiction without the United States.

Section 376. [11 U.S.C. § 776]. If the statement of the executory contracts and the schedules and statement of affairs, as provided by paragraph (1) of section 324 of this Act, are not duly filed, or if an arrangement is not proposed in the manner and within the time fixed by the

court, or if an arrangement is withdrawn or abandoned prior to its acceptance, or is not accepted at the meeting of creditors or within such further time as the court may fix, or if the money or other consideration required to be deposited is not deposited or the application for confirmation is not filed within the time fixed by the court, or if confirmation of the arrangement is refused, the court shall—

(1) where the petition was filed under section 321 of this Act, enter an order dismissing the proceeding under this chapter and directing that the bankruptcy be proceeded with pursuant to the provisions of this Act; or

(2) where the petition was filed under section 322 of this Act, enter an order, upon hearing after notice to the debtor, the creditors, and such other persons as the court may direct, either adjudging the debtor a bankrupt and directing that bankruptcy be proceeded with pursuant to the provisions of this Act or dismissing the proceeding under this chapter, whichever in the opinion of the court may be in the interest of the creditors: *Provided, however,* That an order adjudging the debtor a bankrupt may be entered without such hearing upon the debtor's consent.

#### RULES:

##### RULE 119.

##### BANKRUPT INVOLVED IN FOREIGN PROCEEDING

When a proceeding for the purpose of the liquidation or rehabilitation of his estate has been commenced by or against a bankrupt in a court of competent jurisdiction without the United States, the court of bankruptcy may, after hearing on notice to the petitioner or petitioners and such other persons as it may direct, having regard to the rights and convenience of local creditors and other rele-

vant circumstances, dismiss a case or suspend the proceedings therein under such terms as may be appropriate.

#### RULE 11-17.

##### DEBTOR INVOLVED IN FOREIGN PROCEEDING

Bankruptcy Rule 119 applies in Chapter XI cases.

#### RULE 11-42.

##### DISMISSAL OR CONVERSION TO BANKRUPTCY PRIOR TO OR AFTER CONFIRMATION OF PLAN

###### (a) *Voluntary Dismissal or Conversion to Bankruptcy.*

The debtor may file an application or motion to dismiss the case or to convert it to bankruptcy at any time prior to confirmation or, where the court has retained jurisdiction, after confirmation. On the filing of such application or motion, the court shall—

(1) if the petition was filed pursuant to Rule 11-7, enter an order directing that the bankruptcy case proceed; or

(2) if the petition was filed pursuant to Rule 11-6, enter an order adjudicating the debtor a bankrupt if he so requests, or, if he requests dismissal, enter an order after hearing on notice dismissing the case or adjudicating him a bankrupt whichever may be in the best interest of the estate.

(b) *Dismissal or Conversion to Bankruptcy for Want of Prosecution, Denial or Revocation of Confirmation, Default, or Termination of Plan.* The court shall enter an order, after hearing on such notice as it may direct dismissing the case, or adjudicating the debtor a bankrupt if he has not been previously so adjudged, or directing

that the bankruptcy case proceed, whichever may be in the best interest of the estate—

- (1) for want of prosecution; or
- (2) for failure to comply with an order made under Rule 11-20(d) for indemnification; or
- (3) if confirmation of a plan is denied; or
- (4) if confirmation is revoked for fraud and a modified plan is not confirmed pursuant to Rule 11-41; or
- (5) where the court has retained jurisdiction after confirmation of a plan:
  - (A) if the debtor defaults in any of the terms of the plan; or
  - (B) if a plan terminates by reason of the happening of a condition specified therein.

The court may reopen the case, if necessary, for the purpose of entering an order under this subdivision.

(c) *Notice of Dismissal.* Promptly after entry of an order of dismissal under this rule, notice thereof shall be given as provided in Rule 11-24.

(d) *Effect of Dismissal.* Unless the order specifies to the contrary, dismissal of a case under this rule on the ground of fraud is with prejudice, and a dismissal on any other ground is without prejudice. A certified copy of the order of dismissal under this rule shall constitute conclusive evidence of the revesting of the debtor's title to his property.

(e) *Consent to Adjudication.* Notwithstanding the foregoing, no adjudication shall be entered under this rule against a wage earner or farmer without his written consent.

## Statement of the Case

### A. Background Facts—The Foreign Exchange Contracts and Default.

In January, 1975, Finabank, a Swiss banking corporation, had on deposit approximately \$12,500,000 at the Continental Bank International ("CBI") in New York City. For the most part (about \$11,000,000), this sum of money consisted of cash and certificates of deposit representing the interests of Finabank's customers and depositors throughout the world (App. 88, 98-103). Concededly, none of the funds at CBI belonged to the appellees herein, Chase or FNBB, two large international banks.

In the last days of December, 1974, a single event occurred which precipitated Finabank's insolvency and triggered the question of whether the twelve and a half million dollars on deposit at CBI is to go simply to Chase and FNBB or become part of a pool for all of Finabank's creditors. In late December, 1974, Finabank had outstanding foreign exchange contracts with Edilcentro International Ltd. ("Edilcentro"), a bank in the Bahamas, which were to fall due to Finabank in the first four months of 1975. Finabank, in turn, had previously made foreign exchange contracts with FNBB's Paris branch and Chase's Milan, Italy branch in anticipation that Edilcentro would honor its commitments. In December, however, Finabank was notified by Edilcentro's parent, Societa Generale Immobiliare, an Italian corporation, that Edilcentro would default on the contracts. The loss to Finabank was in excess of \$46,000,000.

It should be emphasized at this juncture that the foreign exchange contracts thus far mentioned were neither negotiated in the United States, nor were they to be performed here. Chase had functioned through an Italian branch in Milan and FNBB acted through its

Paris branch office (App. 7). Thus, in every conceivable respect, the foreign exchange dealings between the parties was of a wholly international character.<sup>2</sup>

Edilcentro's default resulted in Finabank's inability to meet its obligations, including, of course, its foreign exchange contract obligations to Chase and FNBB. Accordingly, Finabank sought immediate relief within the Swiss jurisdiction. On January 10, 1976, pursuant to the laws of Switzerland and the direction of the Swiss Federal Banking Commission, Finabank filed a petition for a "sursis bancaire," a postponement of maturity, in the Courts of the Swiss Canton of Geneva. As was described in Finabank's petition at issue here, the petition filed in Geneva contemplated the rehabilitation of Finabank, but had imposed a moratorium on Finabank's conduct of its business pending, among other things, a determination of its capability for rehabilitation (App. 4).

On January 20, 1975, the Court of Justice of Geneva granted Finabank's petition and constituted FIDES Societe Fiduciaire, a Swiss accounting corporation, as "Commissaire Provisoire" or Temporary Commissioner of Finabank (App. 4). About five months later, on June 19, 1975, Finabank petitioned the Court of Justice in Geneva for a banking moratorium under Article 37 of the Swiss Banking Law (App. 74). The purpose of that

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<sup>2</sup> Although located in Geneva, Finabank was essentially an international bank. Among the 14 bank creditors emerging from Finabank's failure to perform under the forward foreign exchange contracts, only three—including Chase and FNBB—had any serious connection with the United States. That third bank was Firestone Bank, Ltd. of Zurich, Switzerland, which was, at the time, a wholly-owned subsidiary of the Firestone Tire and Rubber Company, which has succeeded to its claim. The remaining creditor banks were from Vatican City, Switzerland, Germany, Sweden, Italy, Luxembourg, Belgium and England (App. 7).

petition was to allow the persons who were to be appointed Finabank's commissioners the opportunity to evaluate its financial condition with a view toward proposing an arrangement with Finabank's creditors (App. 74). On July 14, 1975, the Swiss court granted that petition and designated two additional persons to serve with FIDES as commissioners of Finabank (App. 74).

Finally, on July 9, 1976, having had an opportunity to evaluate Finabank's finances, a third petition was filed with the Swiss courts. This petition was for a "concordat par abandon d'actifs", which, if approved by the court, will ultimately result in a plan whereby Finabank will be liquidated under the supervision of the Swiss Court and commissioners of Finabank's creditors, similar to a creditors' committee, in American bankruptcies. A hearing on the current commissioners' proposed plan to liquidate is presently scheduled to be heard before the Court of Justice of Geneva on November 5, 1976.

#### **B. Proceeding in the United States Including the Filing of the Chapter XI Petition.**

As would be expected, after Edilcentro's default, Chase and FNBB pursued their remedies against Finabank throughout the world. Chase sued Finabank in the Italian courts in Milan and on January 6 and 20, 1975, respectively, Chase and FNBB found and attached Finabank's deposits at CBI in New York City. Chase's attachment was for \$550,000; FNBB's was for more than \$9,000,000, nearly the entire amount that was on deposit at CBI (App. 16-17).<sup>3</sup> Thereafter, CBI commenced an

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<sup>3</sup> The Chase complaint sought \$491,000 for breach of the foreign exchange contracts. It was filed in the Southern District of New York on January 6, 1975 (75 Civ. 39). FNBB's complaint sought \$9,176,375 and was filed on January 20 (75 Civ. 290). (App. 16-17).

interpleader action, *Continental Bank Int'l v. Bank de Financement, S.A.*, 75 Civ. 299 (S.D.N.Y. 1975), to determine the rights of various claimants to certificates of deposit and other funds which CBI was holding for the account of Finabank (App. 18).<sup>4</sup>

On May 5, 1975, in the United States District Court for the Southern District of New York, Finabank filed a petition for an arrangement under Chapter XI of the Bankruptcy Act (App. 1, 3). The timing of the filing was not accidental. By filing the petition on May 5 and not later, Finabank put itself in the position of being able to avoid as a preference the attachments secured less than four months earlier by Chase and FNBB. In effect, Finabank was surrendering its non-custodial assets in the United States to all its creditors to be allocated under American judicial supervision on a *pro rata* basis rather than allowing only two creditors to have them all.

Not surprisingly, Chase and FNBB moved to dismiss the Chapter XI petition and thereby legitimize their preferential attachments at the expense of the creditors at large (App. 10, 77). In support of their motion to dismiss, they argued that the Bankruptcy Act precluded

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<sup>4</sup> The Chase and FNBB actions were consolidated with the interpleader action before Judge Werker on September 19, 1975.

It is Finabank's position in the interpleader proceeding that of the nearly 12.5 million dollars held for Finabank's account by CBI in cash and certificates of deposit, \$11,000,000 represents trust assets held by Finabank as custodian and are not, under any circumstances, a potential pool asset for Finabank's general creditors. See Affidavit of Jacques Girardin (App. 98-103). Finabank, however, recognizes the possibility that many of those deposits may not be claimed by the depositors. Accordingly, those sums which are not properly claimed by depositors should be treated as Finabank's assets. They should not, under any circumstances, fall exclusive prey to the claims of Chase and FNBB.

the filing of a petition by any banking corporation. Secondly, they argued that it was inappropriate (and, hence, dismissible in the discretion of the court) for a foreign bank which had no office in the United States and which did no business here to make a filing under the Act. In this connection, they alleged that the Swiss banking secrecy laws seemingly precluded Finabank from listing with the court all its creditors, customers, and depositors (App. 25). Finally, Chase and FNBB argued that as to the "local creditors" the pending CBI interpleader action provided an adequate forum for the orderly disposition of Finabank funds in the United States (App. 20-21).

### C. Decision of the Bankruptcy Court.

In a decision dated January 12, 1976, Bankruptcy Judge Roy Babitt dismissed the petition on the ground that he did not have jurisdiction over a banking corporation. In support of this, Judge Babitt cited the district court decision in *Israel-British Bank (London) Ltd. v. FDIC*,<sup>5</sup> a decision later reversed by this Court (App. 225).

The bankruptcy court also went on to hold that it had the discretion to dismiss the proceedings for lack of appropriateness and for want of prosecution. On this last mentioned point, which it raised *sua sponte*, the court stated that Finabank was in default in filing its plan of arrangement (App. 229). The court, however, apparently forgot that it had extended that filing deadline to a date in the future (App. 218). No default, technical or otherwise, existed.

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<sup>5</sup> 401 F. Supp. 1159 (S.D.N.Y. 1975), rev'd, 536 F.2d 509 (2d Cir. 1976), *petitions for cert. pending*, 45 U.S.L.W. 3203-04 (U.S., filed Aug. 23, 1976) (Nos. 76-271, 272).

In its decision, the bankruptcy court was not unaware that the primary purpose of the Bankruptcy Act was to insure equality among all creditors. In fact, the court noted, in connection with the petition's having been filed on the eve of the expiration of the four month preference period, that "the impulse and timing of the Chapter XI petition" were "in keeping with Congress' scheme, even in Chapter XI, of equality among all creditors" (App. 228 [citation omitted]).

Having thus cursorily acknowledged the controlling purpose of the Bankruptcy Act, the court inexplicably stated that "it [the court] does not shirk from giving the attaching creditors the advantage over foreign creditors which dismissal of this case will insure" (App. 231). In this connection, it cited the allegedly "well recognized rule between states and nations which permits a country to first protect the rights of its citizens in local property before permitting it to be taken out of the jurisdiction for administration in favor of those residing beyond its borders" (*id.*).

#### **D. Decision of the District Court.**

The order of dismissal was appealed by Finabank to the district court and was heard by District Judge Robert J. Ward on July 13, 1976. In a decision dated July 28, 1976, the district court affirmed the dismissal (App. 277). Noting first that the *Israel-British Bank* case upon which Judge Babitt had primarily relied had been reversed, the district court nevertheless went on to state that the bankruptcy court had properly dismissed the petition in an exercise of its "discretion" (App. 283).

The district court was extraordinarily candid in justifying its decision that the Bankruptcy Judge had properly exercised his "discretion". The court held in sub-

stance, that, as a matter of federal policy, American creditors were entitled, by the very fact of their nationality alone, to recover in full from the assets located here before foreign creditors shared on even a *pro rata* basis. "[D]ismissal" the court stated, "has no adverse effect on the American creditors but to the contrary, represents a step toward assuring that each will recover the sums due them without having to rely on Swiss bankruptcy procedures which are enmeshed with the Swiss bank secrecy laws. . . . [T]he claims of local creditors appear best protected by dismissal of the case." (App. 282-283).

Unlike the bankruptcy court decision, the principle of equality among creditors was not even accorded recognition by the district court. Thus, this Court's recent decision in *Israel-British Bank* permitting a foreign bank to take advantage of the Bankruptcy Act for the purpose of insuring equal distribution among all creditors was emasculated. The district court established a new rule that bankruptcy judges are permitted to dismiss proceedings or, by fair extension, take any other action in order to insure that Americans are preferred over other nationals.

### Summary of Argument

The decisions of both the district and bankruptcy judges are bottomed on a xenophobia which is alien to the Bankruptcy Act's policy of equal treatment among creditors and which is contrary to this Court's recent decision in the *Israel-British Bank* case. There has been no reasoned showing why Chase and FNBB should receive more than their fair share of Finabank's assets. Moreover, there has not been any showing that they would not be treated on an equal footing with Finabank's other creditors under the auspices of a dual Swiss and American administration of Finabank's affairs. To per-

mit the decision of the district court to stand will eliminate, in multinational corporate insolvencies, any salutary contribution by American bankruptcy courts. In addition, if permitted to stand, the decision will likely result in harm to American economic interests.

Once it is recognized that the decision of the district court is erroneously premised, it can be seen that there is no discretion under any of the Bankruptcy Act's Sections or Rules to dismiss this petition. Thus, there is no "inherent power" to favor local creditors to the detriment of foreign creditors any more than there is such discretion conferred under Section 2(a)(22) and Rule 119 which, although they speak of the "rights" and "convenience" of local creditors, were never intended to create exclusive rights on behalf of self-styled local American creditors.

Finally, dismissal under Rule 11-42(b), without a hearing, was altogether erroneous. Had such a hearing been held, and the court was satisfied that no plan could be formulated, then it should have adjudicated Finabank a bankrupt. Outright dismissal of the petition with the concomitant validation of FNBB's and Chase's preferential liens, was an unjust infringement upon the rights of all the other creditors entitled to share in Finabank's assets.

## ARGUMENT

## I

**There is no discretion to dismiss an arrangement where the sole effect of dismissal is to confer a preference on one class of creditors.**

The Court is called upon in this case to clarify, and we submit reaffirm, the meaning of its recent decision in *Israel-British Bank (London) Ltd. v. FDIC*, 536 F.2d 509 (2d Cir. 1976), *petitions for cert. pending*, 45 U.S.L.W. 3203-04 (U.S., filed Aug. 23, 1976) (Nos. 76-271 & 272). Despite some mention below that the case involves the technical interpretation of several sections and rules of the Act, the case really turns on a broad question of policy: IS the Bankruptcy Act's main purpose—equality of distribution among creditors—superseded by a chauvinistic policy of preferring American creditors over foreign creditors, when the bankrupt is not an "American" but has some of its assets here and where the bulk of the creditors appear to be "foreign".

We believe that *Israel-British Bank* makes clear that the Act's main purpose—that of creditor equality—should not be ignored in favor of narrow parochial ends. Instead, the Act's mandate of creditor equality must be implemented to accommodate increasingly international dealings and ownerships of foreign and domestic corporations.

We start off, then, with the factor which was disregarded by the district court in reaching its decision. More than a hundred years ago, the Supreme Court stated: "The primary object of a bankruptcy law is to

secure a just distribution of the bankrupt's property among his creditors. . . ." *Wilson v. City Bank*, 84 U.S. (17 Wall.) 473 (1873). It has been repeatedly recognized that "[t]he main purpose of the bankruptcy law is to prevent preferences and secure a fair and equitable division of the bankrupt estate among the creditors. . . ." *In re Leslie*, 119 F. 406 (S.D.N.Y. 1903); 3 *Collier on Bankruptcy*, ¶ 60.01 & *id.* at 743 n.1 (1975) (and cases cited therein). This fundamental point cannot legitimately be given only the short shrift it was accorded by the lower courts.

The position of the district court is particularly insensitive to the position of Finabank's other creditors in view of this Court's recent decision in the *Israel-British Bank* case. In that case, the question (one of first impression) was whether the Bankruptcy Act should be interpreted so as to permit a foreign bank, which (as Finabank) did no business in the United States, to avail itself of the protections of the Act. The issue was created by virtue of the exceptions listed in Section 4a of the Act, which includes a "banking corporation."<sup>6</sup> The factual setting for the issue was, in many respects, identical to the factual setting here. Thus, although the Israel-British Bank ("IBB") did no business here, it did maintain deposits in U.S. banks. Similarly, IBB defaulted on obligations to U.S. banks which, subsequently, attached the bank's deposits. Sometime before the end of four months, IBB filed a voluntary petition in bankruptcy which would have enabled IBB's American trustee to avoid the attachments. Bankruptcy Act § 67a(1), 11

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<sup>6</sup> Section 4a, 11 U.S.C. § 22a, provides:

"Any person, except a municipal, railroad, insurance or banking corporation or a building and loan association, shall be entitled to the benefits of this Act as a voluntary bankrupt."

U.S.C. § 107(a)(1).<sup>7</sup> As this Court stated, the practical effect of adversely determining the jurisdictional issue was: "If there is no jurisdiction to entertain a voluntary bankruptcy petition for IBB, the liens will be good, and appellees [local banks] will fare better than United States creditors—among others." 536 F.2d at 511.

There seems little doubt that the holding of the *Israel-British Bank* case, which was to sustain jurisdiction, was a direct outgrowth of this Court's desire to avoid unequal distributions, for it stated:

The theme of the Bankruptcy Act is equality of distribution of assets among creditors, *Samp-*

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<sup>7</sup> Prior to filing the petition, IBB filed a debtor's petition in England. Thereafter and subsequent to the filing of the petition, the High Court of England directed the appointment of American counsel to insure that IBB's assets in this country become available for the "benefit of creditors general" (536 F.2d at 511). Accordingly, this Court stated (*id*):

"We take the bankruptcy proceeding here to be in aid of the order of the High Court that the assets in the United States become available to creditors on the basis of equality."

Appellees herein do not, nor could they, claim that the Swiss courts would not similarly make Finabank's American assets "available to the creditors on the basis of equality." In fact, in a decision of the First Section of the Court of Justice of the Canton and Republic of Geneva, dated July 14, 1975, in *In re Banque de Financement, S.A.*, a translation of which will be provided to the panel which will hear argument in this case, There was entered an order in which the Court, in one of its decretal paragraphs, stated:

"The Court:

\* \* \* \* \*

"Instructs the commissioners to take all necessary measures to preserve the assets and to prevent that certain creditors be favored to the detriment of others, unless with the latters' agreement."

*sell v. Imperial Paper & Color Corp.*, 313 U.S. 215, 219, 61 S.Ct. 904, 85 L.Ed. 1293 (1941); *Buchanan v. Smith*, 83 U.S. (16 Wall.) 277, 301, 21 L.Ed. 280 (1873); 3 Collier on Bankruptcy ¶ 60.01, at 743; see *Young v. Higbee Co.*, 324 U.S. 204, 210, 65 S.Ct. 594, 89 L.Ed. 890 (1945), and correlatively avoidance of preferences to some. 1 Remington on Bankruptcy § 17, at 34 (5 ed. J. Henderson 1950). The road to equity is not a race course for the swiftest. 536 F.2d at 573.

The Court in *Israel-British Bank* was also mindful that "... United States creditors could be harmed if preferential liens were permitted to survive. . . ." Thus, by sustaining jurisdiction this Court recognized that "[I]n so doing, we avoid an inequitable result to [IBB's] creditors, including the other American banks who have lost the race of diligence."<sup>8</sup>

The point of *Israel-British Bank* has been entirely missed by the district court. There is not one word in the opinion below which recognizes that the dominant purpose of the Act is to foster equality among all creditors, not simply American creditors. Instead, the opinion frankly exalts regional chauvinism, undermines equality of distribution and thereby completely undercuts the *Israel-British Bank* case.

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<sup>8</sup> In this case, the First National City Bank lost the race of diligence on its claim of \$138,000. (App. 20). Judge Ward, however, in a kind of perversion of the aphorism "the greatest good for the greatest number" remarked that First National City Bank's claim was "relatively minor" and therefore "dismissal has no adverse effect on American creditors. . .". (App. 282). In addition, the Firestone Tire and Rubber Company, which owned all of the outstanding stock of Bank Firestone (now dissolved), apparently stands to lose more than a half million dollars if the petition is dismissed. Judge Ward ignored that fact completely.

The difficulty, of course, lies in the district court's understanding of Section 2a(22) and Bankruptcy Rule 119. Section 2a(22) provides that courts of bankruptcy may:

Exercise, withhold, or suspend the exercise of jurisdiction, having regard to the rights or convenience of local creditors and to all other relevant circumstances, where a bankrupt has been adjudged bankrupt by a court of competent jurisdiction without the United States.

Rule 119 provides:

When a proceeding for the purpose of the liquidation or rehabilitation of his estate has been commenced by or against a bankrupt in a court of competent jurisdiction without the United States, the court of bankruptcy may, after hearing on notice to the petitioner or petitioners and such other persons as it may direct, having regard to the rights and convenience of local creditors and other relevant circumstances, dismiss a case or suspend the proceedings therein under such terms as may be appropriate.

The decision of the district court interprets these provisions in a manner which is both contrary to their purpose and which, as we will show, is absolutely unworkable.

The district court, in effect, has taken the phrase "rights of local creditors" to mean that local creditors are to be preferred over foreign creditors. This is plainly wrong. As counsel for intervenor Firestone Tire and Rubber Company has so ably argued (Brief at 19):

... the purpose of § 2a(22) and Rule 119 is to enable the American proceeding to be dismissed or suspended in favor of the foreign proceeding in order to avoid duplicate administration of a bankrupt's estate where it would be wasteful of

time and expense [footnote omitted] but only provided it is utilized in a manner that will not result in permitting *preferential attachments* of the American assets to stand. If there have been local preferential attachments of the American assets, an American bankruptcy proceeding is entirely proper for the purpose of preserving those assets for the estate by setting aside those attachments, *even if that is the sole purpose of the American proceeding*. In fact, in those circumstances, § 2a(22) and Rule 119 were not intended to afford the bankruptcy court discretion to dismiss the American proceeding.

The point is fundamental because, once again, the Act's policy of equal distribution comes into play. As Professor Nadelmann has stated:

When local assets are attached after bankruptcy has been declared abroad and the foreign trustee is not permitted to collect the assets because of the attachment, a local bankruptcy adjudication becomes indispensable to secure equal distribution of the attached assets among all creditors. No room is left for the exercise of discretion by the bankruptcy court in favor of the foreign proceeding. Nadelmann, *The National Bankruptcy Act and the Conflict of Laws*, 59 HARV. L. REV. 1025, 1046 (1946).<sup>9</sup>

It is manifest, therefore, that when Rule 119 directs courts to have "regard" for the "rights" and "convenience" of local creditors it means something quite different

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<sup>9</sup> Intervenor has so thoroughly examined the background of § 2a(22) and the unique contributions of Professor Nadelmann, that Finabank will not add to Firestone's treatment and adopts the argument. FED. R. APP. P. 28(i).

than appellees would have it mean. Indeed, the most sensible interpretation of the Rule and the Section would also be consistent with the policy of equality. Such an interpretation would be that the dismissal or suspension of a bankruptcy proceeding in the United States is appropriate only where to do so would not affirmatively work to harm or impede the claims of local creditors who, because their situs is in the United States, might find it difficult or inconvenient to pursue their claims in the foreign jurisdiction.

Stated differently, the Rule means that local creditors may properly have standing to urge the court *not* to dismiss or suspend. But local creditors are not conferred with standing to maintain a position in favor of dismissal for, if they were, equal distribution in foreign bankruptcies—as exemplified in the *Israel-British Bank* case—would be a meaningless goal and Section 2a(22) could just as well never have been enacted.

Moreover, a narrow, xenophobic interpretation of Section 2a(22) and Rule 119, even if consciously adopted as federal policy, would be unworkable. If it were assumed, as the court below held, that “regard” for “local creditors” means that the claims of American corporations against foreign entities (in appellee’s formula corporations and persons would have to be included as well as banks because § 2a(22) makes no distinctions along those lines) are to be treated on a preferred basis, absurd results would follow.

Suppose that in this case Finabank was wholly owned by the General Motors Corporation and that FNBB was wholly owned by the country of Iran. Suppose further that Chase was wholly owned by a wealthy American family, fully domiciled in the United States. Also, imagine that two so-called American corporations lost the “race

of diligence" and stand to lose over \$700,000 if the attachments are not dissolved. Finally, imagine that Iran owes General Motors \$10,000,000 for a large delivery of trucks.

Should the petition be dismissed on the theory that Iran, the ultimate beneficiary of FNBB's attachment, will thereby be provided funds to pay General Motors for the trucks it has purchased? Should dismissal follow because Chase, in the example, is owned by an American family? Should it make a difference if one family member is not domiciled in the United States? Conversely, should the petition be retained because two American corporations have lost "the race of diligence" but dismissed if it is found out at a hearing that those two corporations are, in fact, owned by foreign interests?

All of these questions, of course, could be extended. The permutations are inexhaustible and inevitable. Indeed, the situation in the case at bar actually contains some of the phantom-like features of the example. Although on first glance both FNBB and the Chase may be called "American", in truth it was FNBB's Paris branch and Chase's Italian branch that entered into the foreign exchange contracts in Europe which are the basis for the claims against Finabank by these two "American" banks. In this context, are FNBB and Chase really "American" banks? And why should those two "Americans" take precedence over Citibank and Firestone?

How does one accurately spot a "local" creditor, particularly when the creditors are multinational corporations. Or, are "local" creditors really only illusions.

What test is to be employed if our ultimate aim is to protect "local creditors" (or, crudely translated, "protect our own")? The question answers itself. In our

modern world, there is no way of extrapolating from the normal, complicated relationships and ownerships of large, international banks and corporations (or other forms of business entities) an answer which could possibly satisfy the narrow and short-sighted policy urged below by appellees.

The reality is that there is an international business community, particularly involving international financial institutions, that depends upon, for its survival and vigor, a broad complex of interdependent relationships. The international comity and cooperation that must surround this financial community obviously must extend to, and be reflected in, internal legal systems, and more particularly to notions and rules of bankruptcy and just administrations of bankrupt estates. An American bankruptcy law which does not recognize, take into account and actively foster equality among American and non-American creditors is archaic, incompatible with concepts of internationalism, and, finally, invites retaliation by other legal systems.

There is no persuasive reason to permit Chase and FNBB to gain the tremendous advantage they are gaining from this dismissal over the Firestone Tire and Rubber Company or Citibank. *Israel-British Bank (London) Ltd. v. FDIC.*, *supra*, 536 F.2d at 515. And, because there is no workable test that can isolate "American" interests, there is no persuasive argument to permit Chase and FNBB an advantage over other international entities. In short, there is no sound reason why equality of treatment should be read out of Section 2a(22) and Rule 119. Consequently, there was no discretion to dismiss the petition.

## II

**If a successful arrangement appears unlikely, the proper remedy is adjudication, after a hearing to determine the actions which will best protect all creditors.**

Although the district court, clearly, and quite candidly, bottomed its decision on a policy rationale that would prefer American creditors over foreign creditors, the court in passing raised several other issues. These other issues, more in the nature of window dressing, can be dealt with briefly.

### **1. Alleged failure to file a Plan:**

The bankruptcy court stated that Finabank was in default in filing a plan of arrangement, but the district court avoided a finding on this (App. 229, 280). The reason for the district court's avoiding the issue is clear. The bankruptcy court, when it wrote its decision and raised *sua sponte* the failure to file a plan, apparently forgot that it had granted Finabank an extension of time to file the Plan. In fact, at the time of the bankruptcy court's decision, Finabank had two weeks more to file its Plan (App. 218).

It is difficult to comprehend how an error by the court can not only be ignored but transformed into a basis upon which to predicate a decision that the court acted properly. Certainly, all of Finabank's general creditors should not be penalized and deprived of any recovery whatsoever out of United States assets because of an error by the court.

Beyond that, it is clear that, even if a plan had not been timely filed or if the court for any other reason

thought the action was not being prosecuted, the court was under a *duty* to hold a hearing and make a determination as to whether to dismiss the proceedings or adjudicate Finabank a bankrupt, whichever would be in the interest of the creditors as a whole. The decision whether to dismiss or adjudicate, according to Rule 11-42 of the Bankruptcy Rules, depends upon "*whichever is in the best interest of the estate.*" The court could never have reached its determination to dismiss the proceedings rather than to adjudicate Finabank a bankrupt had it followed the guidelines of Rule 11-42. The test to be used is what would be in the best interests of the estate—or as Section 376(2) of the Act and the Advisory Committee's notes to Rule 119 state—the best interest of "*the creditors.*"

"Creditors" does not mean local or American creditors. It means all the creditors. But by dismissing the petition and thereby reinstating the attachments, the bankruptcy court knew it was favoring two creditors—Chase and FNBB—and depriving all the remaining creditors of any chance of recovery. How could this be considered in the best interest of the estate? Clearly, the bankruptcy court should have adjudicated Finabank a bankrupt, voided the attachments, and treated all general creditors equally.

This alleged issue about whether or not Finabank failed to timely file a plan actually brings into focus a fundamental question about the Bankruptcy Act and the role of the bankruptcy court. As noted in Point I, *supra*, the primary theme of the Bankruptcy Act is equality among creditors and fair distribution of the bankrupt estate. And in carrying out this policy, the bankruptcy judge, unlike what might be said to be the impartial neutrality of a district judge in a civil or criminal case, has an affirmative duty to be actively involved in the process.

The bankruptcy judge is a partisan, who must insure that creditor equality and fair distribution is actually implemented. In part, this is because in the normal case many creditors of the estate will not, and cannot be expected to, become actively involved in the process. Therefore, concepts of punitive action are, in large measure, inappropriate in a bankruptcy context.

Thus, even if there had been a failure to file a timely plan, or for that matter some other alleged dereliction on the part of Finabank was involved, the proper remedy would not be a punitive dismissal, which may or may not have been appropriate in a civil or criminal case, but rather whatever action the bankruptcy judge believed was necessary to best protect the general creditors of the estate as a whole. In this case that would have been an adjudication of bankruptcy, which would have treated all creditors equally, and not a dismissal which was calculated to give two large banks preference over other creditors (both foreign and American) (see App. 187).

## **2. Ability of Finabank to be rehabilitated:**

The bankruptcy court found and the district court affirmed that there was little or no chance of rehabilitating Finabank. Both base this finding on remarks made "with commendable candor" (App. 226) by Finabank's counsel that a plan might be impossible to achieve, although attempts were still being made to effect one. From such statements by counsel, the court concluded that it would be impossible to propose a plausible plan.

The record shows that attempts were being made to arrive at a joint plan in Switzerland and the United States (App. 74, 180, 186). Notwithstanding this, the court had no justification to dismiss the proceedings there-

by penalizing all the creditors except the two U.S. chartered multinational banks. It is obviously the other creditors, not Finabank, who suffer from the dismissal.

Finabank, by filing a petition under the Act in the first instance, was well aware that it would eventually have to surrender most, if not all, of its assets. Its position is not changed one iota if it gives all its money to two creditors as opposed to all the creditors. It is the general unsecured creditor—the person whom the Bankruptcy Act was designed to protect—who suffers by the dismissal. And it is because Swiss law, as English law in *Israel-British Bank*, (see footnote 7, *supra*, at 17) requires that Finabank protect its general creditors, that counsel has been retained in the United States to file and defend the petition herein.

Again, if the Court came to the conclusion that Finabank could not have been rehabilitated, then it should have done what it does in every other case—*i.e.*, adjudicated it a bankrupt. The only purpose for a dismissal, conceded by all, was to give the two American banks more than that to which they were entitled. Obviously, as argued in Point I, *supra*, Finabank disagrees with this policy approach of calculated discrimination. But again, the supposed issue of whether or not Finabank could have been rehabilitated is a straw man, because if the Bankruptcy Judge firmly came to that conclusion he should have protected all creditors by adjudicating Finabank a bankrupt, not dismissing to prefer two creditors.

### 3. Swiss Banking Secrecy Law

Although there never was a hearing, and thus never any finding as to how the fabled Swiss Secrecy Law would apply in the instant facts, Chase and FNBB have raised

the spectre that the bankruptcy court would, if it did not dismiss, be compelled to make payment to alleged creditors who, for whatever reason, would refuse to identify themselves or their underlying relationship with Finabank. Unfortunately, it is evident from their decisions that the bankruptcy court and the district court were similarly frightened by this unexplored and speculative area.

Of course, no such thing should ever happen. Any number of safeguards are available to insure the bankruptcy court that a particular claim is a bona fide one. The best illustration is the method devised by Judge Werker in the CBI interpleader action where some certificate of deposit holders were reluctant to come forward and disclose their identities:

Claimants must demonstrate that they deposited funds with Finabank and that Finabank then invested those funds as an agent in certificates of deposit or participations thereof. Specifically this would consist of advices from Finabank to the principal as to the receipt of funds and also advices from Finabank indicating that those funds have been invested in certificates of deposit or parts thereof specifying the number of the certificate corresponding to a numbered certificate held by CBI. This much evidence is required in order to insure CBI against liability which might arise out of payment of the funds to persons not rightfully creditors of Finabank. Any privileges of secrecy accorded by means of numbered accounts by foreign law must in this instance be given a subordinate position to the right of the interpleader plaintiff to be free from being subjected to duplicative or conflicting claims as to any particular account. Numbered accounts as revealed in Finabank's records are insufficient for

poses of a definitive determination as to who the owners of the certificates are, and the court need not accept the records of the Commissioners of Finabank which refer only to account numbers. Records by number alone are subject to error. In addition, in order to properly render judgment disposing of sums on deposit with Finabank, the court must be able to refer to named parties. Finabank is therefore directed to advise its depositors as to the requirements set out by this opinion. In the event that such depositor-claimants fail to answer and move for summary judgment within a reasonable period of time after they have filed an answer with the required evidentiary proof, such funds will be subject to forfeiture.<sup>10</sup>

At the very worst, those creditors who will not reveal their identities recover nothing (App. 178). As a result, the fund for the remaining creditors would be larger.

While Judge Werker's procedure is certainly not the only possible approach, it is far superior to having two creditors obtain all of Finabank's United States assets and the remaining creditors none, which is the net result of appellees specious contention that the "interpleader action will provide a forum for the orderly disposition of the funds . . ." (App. 21). Plainly, the only "order" in such a proceeding is that the other creditors are excluded.

Once again, the issue of Swiss banking secrecy is a false one. First of all, the bankruptcy court should have held a hearing to determine the real facts about the operation of Swiss banking law. Among other things, it would have found that under Article 10, ¶ 20 of the

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<sup>10</sup> A copy of Judge Werker's opinion will be provided to the Court prior to argument.

Swiss Federal Supreme Court Ordinance of April 11, 1935, a list of creditors of a bank in the preliminary stages of liquidation (such as Finabank) can be obtained by any creditor who shows a legitimate interest in procuring it; that the commissioners of such a bank have full access to all of its files; and that its creditors commissioners also have such access. Of course, just as is possible in American discovery proceedings, orders are sometimes made limiting access to such information to lawyers for the parties.

Beyond this, if some aspect of Swiss banking secrecy were found troublesome by the bankruptcy court, the court could then have, as did Judge Werker, fashioned an appropriate remedy. The draconian remedy of dismissal, to prefer the two American banks, based on a *supposition* about Swiss bank secrecy, is not the appropriate remedy when the rights of creditors as a whole are so clearly prejudiced.

#### 4. Summary

Actually, the lower court's discussion of these secondary issues underscores a fundamental failure of the bankruptcy judge to comply with the Bankruptcy Act's procedural requirements. Both Rule 11-42 and Section 376 of the Bankruptcy Act require a *hearing* prior to dismissal. The purpose of that hearing is to determine what remedy is the one which best suits the interests of the creditors as a whole. And it is only after such a hearing that the bankruptcy court can properly fashion relief, for only at that time will the court have before it all the facts concerning the problems of creditor notice, the alleged impact of Swiss banking secrecy on the claims of American creditors abroad, and the prospects for rehabilitation.

No such hearing was held in this case. And the only reason for failing to hold a hearing was that the lower courts had resolved to decide the case so that so-called American creditors would be preferred over all others. That was a reversible error.

### **CONCLUSION**

**For all the foregoing reasons, the order appealed from should be, in all respects, reversed and the case remanded to the Bankruptcy Judge with instructions that Finabank be adjudicated a bankrupt.**

Dated: October 1, 1976

Respectfully submitted,

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Laura Roger , being duly sworn deposes  
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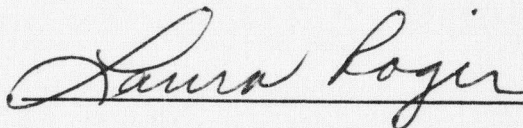
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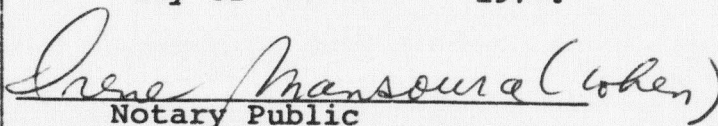
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Notary Public

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